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Real World

Finance and Real Estate News

In this issue

HEADNOTE

Life after the crisis

by **Ciaran P. Carvalho**

The momentous events of the last few weeks have been staggering. The financial crisis is severe and its effects will be wide-ranging. But around the world, governments are showing a determination to do whatever it takes not to allow the banking sector to fail and they are backing that determination with a huge financial commitment. Gradually, these measures should restore confidence in the banking system, with a positive knock-on effect on the whole financial sector and the wider economy.

Certainly life, and business, will go on after the crisis, but what will the finance and real estate world look like once the dust has settled and we start to see the return of investor confidence and the financial markets begin to function normally again? Activity may resume first in the form of workouts and loan modifications (perhaps at a price), as businesses pick up the pieces of deals negotiated in better times. It is widely expected that in place of the largely unregulated excesses of the last few years, there will be a return to more traditional banking with lending at 65% to 75% loan-to-value ratios and generally a more conservative and cautious approach. There will be a push towards more transparency, perhaps with the use of simpler and less complex structures. Investors and financiers will want to understand exactly what they are getting into and to be able to quantify the risks involved. For some, perhaps institutions and less leveraged buyers sitting on equity capital, the falls in capital values and increased yields will present opportunities to pick up good bargains.

Meanwhile, in this issue we have a round-up of finance and real estate news and articles on the wording of guarantees, covenants that require the approval of proposed works and a provision in the Planning Bill that will allow minor changes to planning permissions without requiring further public consultation.

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CONTRACTS

Covenants – whose approval is needed?

by **David Gervais**

Properties are often subject to covenants requiring works to be approved by another person. Sometimes it is not clear whose approval is needed, or whether approval is still needed at all.

The issue came to the fore recently in the case of *Margerison v. Bates*. The case concerned a bungalow built in the garden of a large house in Cheshire but the issues raised might apply equally to commercial owners and developers. When the land for the bungalow was sold in 1966, the owner of the house imposed a restrictive covenant preventing any alteration to the bungalow without the plans having first been approved by "the vendor". In 2007, the owner of the bungalow wanted to replace the flat roof with a pitched roof. By then, the house had been sold and the original owner had died. The new owners of the house objected to the works and claimed they had the benefit of the covenant.

The court considered the wording of the conveyance that contained the covenant and decided that the reference to "the vendor" was not intended to include future owners of the house. Therefore, only the original house owner had the right to approve alterations.

This might not apply in every case; it will depend on the wording of the document that imposes the covenant. In the *Margerison* case, other clauses of the document referred to future owners, which suggested that the benefit of the covenant was deliberately limited to the original owner. As the wording was clear on that point and did not produce an absurd result, it was not possible for the court to decide, as it had in other cases, that a reference to future owners was implied.

As the original owner had died, the court then had to decide whether the covenant was discharged, so that approval was no longer needed, or whether the covenant became absolute, so that no alterations were permitted.

In deciding that point, the court considered the earlier case of *Crest Nicholson Residential (South) Ltd v. McAllister*. In that case, the company that had to approve the works had been dissolved. The court decided that the original parties would not have intended the covenant to become absolute, as that would prevent any further development. So the court implied a term into the covenant that if the company were dissolved, the covenant would be discharged.

Applying that reasoning to the *Margerison* case, the court concluded that, as the purpose of the covenant was to give the original owner of the house some control over alterations, not to prevent them, the parties could not have intended the covenant to prohibit all alterations once the original owner died. The effect was, therefore, to discharge the covenant.

A number of practical points emerge from these cases:

- The right to approve works does not necessarily pass to a new owner—it depends on the wording used and what the court perceives to have been the intention of the original parties.
- If the person having the right to approve the works no longer exists, the covenant is likely to be discharged so no approval is required, but again it depends on the wording of the particular document and what the original parties intended.
- When buying property from a party who will retain the right to approve works, buyers should try to obtain the seller's agreement not to approve works without the buyers' consent.
- When negotiating new covenants, current owners should make clear whether or not the right to approve works will pass to future owners and what is to happen if the person with the right to approve works no longer exists.

Sources: *Margerison v. Bates [2008] EWHC 1211 (Ch); Crest Nicholson Residential (South) Ltd v. McAllister [2002] EWHC 2443 (Ch).*

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PLANNING

Minor changes to planning permissions

by **Priyesh Patel**

Local authorities often agree to minor modifications required by developers even after having issued a valid planning permission. The court has confirmed their power to do this where the changed development would not be substantially different from what was applied for—the so-called "Wheatcroft test". But in allowing changes without public consultation, the authority could be risking accusations of bias or threats of judicial review. The Planning Bill, currently going through Parliament, will for the first time put the power to make changes that are not material on a legislative footing.

The *Wheatcroft* case suggests that the test to be applied in deciding whether changes may be permitted without a further planning application is whether the amendments would result in something "*substantially different from the development applied for*". However, the case also emphasized the need to consider whether further public consultation is needed. The judge said: "*The main . . . criterion upon which . . .judgment was to be exercised was whether the development was so changed that to grant it would be to deprive those who should have been consulted on the changed development of the opportunity of such consultation*".

Later cases have also stressed the importance of public participation in the planning process. Lord Hoffman said in *R v. East Sussex County Council, ex parte Reprotech Ltd in 2002: "It is clear . . . that a determination is not simply a matter between the applicant and the planning authority in which they are free to agree on whatever procedure they please. It is also a matter which concerns the general public interest and which requires . . . the public itself to be able to participate*". His words were quoted in the later case of *Henry Boot Homes Ltd v. Bassetlaw DC*, which concerned the variation of a planning condition. The judge said that planning law was not a matter for private agreement between developers and local planning authorities.

So the test can be rephrased as: does the public need to be consulted? If so, then a further planning application is required; if not, then permission for the amendment can be granted.

The risk for local planning authorities in relying on this rather uncertain test is that they may be vulnerable to accusations of bias towards developers or even threats of judicial review for a breach of natural justice.

Greater certainty is set to be introduced by the Planning Bill, which is currently in the House of Lords. The Bill has mainly attracted attention because it deals with the introduction of the community infrastructure levy and the new regime for planning permission for nationally significant infrastructure projects. But it also includes clause 184, which will insert a new section 96A into the Town and Country Planning Act giving local planning authorities the power to make a change to a planning permission if they are satisfied that the change is "not material". Relying on this statutory authority instead of the *Wheatcroft* test should reduce the risk of judicial review.

Sources: *Bernard Wheatcroft Ltd v. Secretary of State for the Environment [1980] 43 P &CR 233; Pioneer Aggregates Ltd v. Secretary of State for the Environment [1985] 1AC 132; R v. East Sussex County Council, ex parte Reprotech Ltd [2002] 4 ALL ER 58; Henry Boot Homes Ltd v. Bassetlaw DC [2002] ALL ER (D) 421; Planning Bill clause 184.*

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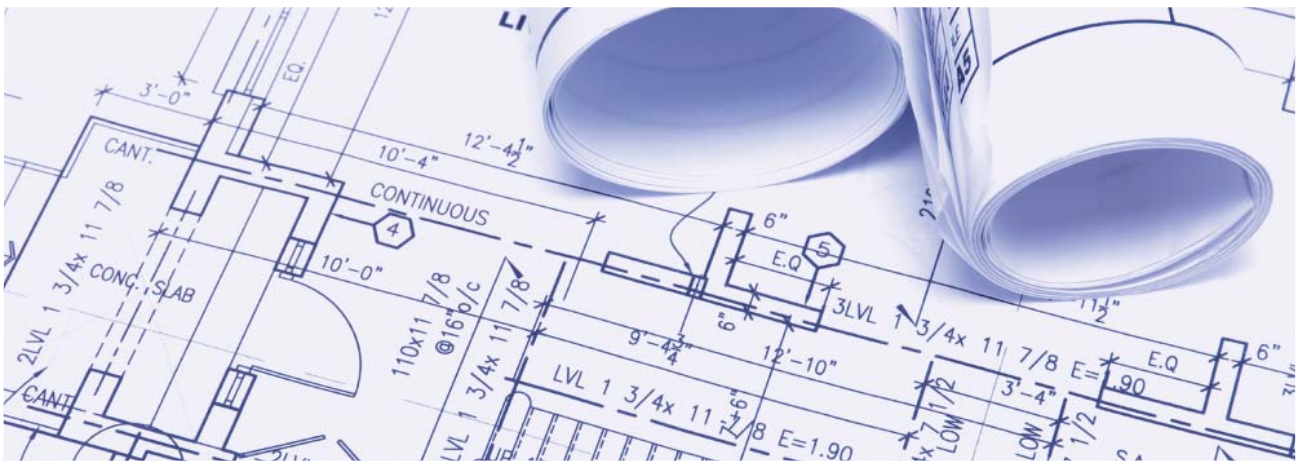

GUARANTEES

Have I provided a guarantee or a performance bond?

by **Catherine A. Stringer**

The recent case of IIG Capital LLC v. Van Der Merwe *has highlighted the risk that what is described as a guarantee may in fact amount to a performance bond. A guarantee is a secondary obligation, which means that the guarantor cannot be required to pay more than the liability under the original contract. However, a performance bond is a primary obligation that is payable on demand, irrespective of liability under the original contract. The case confirmed that it is essential, particularly for company directors, to look carefully at the terms of any guarantee that they are asked to provide to ensure they are not inadvertently taking on more liability than expected.*

Facts

IIG Capital LLC ("IIG") entered into a loan agreement with Hurst Parnell Imports and Exports Ltd ("HPIE"). As security for the loan, HPIE granted a debenture over its assets and the directors of HPIE, Mr. and Mrs. Van Der Merwe (the "Guarantors"), each provided a guarantee in favour of IIG.

In January 2007, IIG demanded US$30,303,576 from HPIE, claiming it was due under the loan agreement. HPIE did not pay the sum demanded and four days later IIG wrote to the Guarantors stating that HPIE had failed to pay, certified that the amount was due and payable by the Guarantors and demanded payment within two days. The Guarantors did not pay.

IIG applied for judgment against the Guarantors. The Guarantors argued that, as guarantors, they had a secondary liability and were entitled to rely on defences which could have been raised by HPIE in resisting the claim for payment under the loan. The case went to the Court of Appeal.

The court's decision

The Court of Appeal decided that the guarantees amounted to performance bonds and the Guarantors were bound to pay on demand the amount certified as due by IIG and could not raise defences available to HPIE.

The court held that there is a strong presumption against a guarantee entered into by an individual being construed as a performance bond, but the presumption can be rebutted if there is clear wording to that effect in the document.

Here, each Guarantor as "*principal obligor and not merely as surety*" guaranteed the due and punctual payment by HPIE of "all monies due owing or payable *or expressed to be due owing or payable*" to IIG . If such monies were not paid in full on the due date, the Guarantors would "*immediately upon demand unconditionally*" pay to IIG the unpaid amounts. The words in italics indicated to the court that the Guarantors were taking on more than a secondary obligation.

This was put beyond doubt by a later clause that provided that a certificate in writing from IIG stating the amount at any particular time due and payable by the Guarantors would be binding on the Guarantors save in the case of manifest error. A manifest error is one which is "obvious or easily demonstrable without extensive investigation" and did not apply here.

Action

Guarantors and their advisors should make clear in the guarantee that it is not a performance bond and reserve the right to raise any defences against liability available to the original contracting party.

Sources: *IIG Capital LLC v. Van Der Merwe and another [2008] EWCA Civ 542*

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REAL ESTATE

Real World roundup

by **Gillian Baxter**

Now *nearly* all buildings need energy performance certificates

In our Spring edition, we reported on the phased introduction of energy performance certificates for commercial buildings. At first they were only required for buildings over 10,000 sq. m. That limit was reduced to 2,500 sq. m. in July but transitional provisions exempted properties already on the market. 1 October saw the start of the final phase: now a certificate must be provided on the sale, leasing, construction or modification of virtually all commercial buildings. However, new regulations provide that properties already on the market on 1 October will not need a certificate until they are sold or let or until 4 January 2009 at the latest. The regulations also extend the shelf life of residential energy performance certificates from one to three years.

There are still some minor exceptions where certificates are not needed—places of worship, temporary buildings expected to be used for less than two years, stand-alone buildings with a useful floor area less than 50 sq. m., industrial and agricultural buildings with a low energy demand and buildings due to be demolished.

Source: *the Energy Performance of Buildings (Certificates and Inspections) (England and Wales) (Amendment No. 2) Regulations 2008.*

Surveyor has absolute duty to value the correct property

The Court of Appeal has decided that a valuer has an absolute obligation to value the correct property. As a result, a surveyor who was tricked into inspecting the wrong house was liable in damages to the lender to compensate for a shortfall in the sale proceeds when the correct property was sold. Usually surveyors and other professionals are only required to exercise the degree of skill and care in providing their services that would be expected of a reasonably competent professional in their field, but the obligation to inspect the correct property is an exception to that general rule.

Source: *Platform Funding Ltd v Bank of Scotland plc [2008] EWCA Civ 930.*

Compulsory purchase compensation windfall

Amid the economic doom and gloom, one landowner has cause to celebrate. In 2001, it bought land used as public open space for £30,000 hoping to develop it. Following service of a purchase notice, the Court of Appeal upheld an award of compensation of £1.6 million, on the assumption that the land had planning permission for nine houses and a commercial building, rather than the £15,000 it was worth for use as public open space.

The decision results from a statutory assumption that planning permission would be granted to rebuild buildings on the land before 1 July 1948 and demolished after 7 January 1937. Nine houses and a commercial building had stood on the land until they suffered war damage, so the valuation had to assume there was planning permission to rebuild them. The provisions are a hangover from the time when there was blanket permission for the rebuilding of war damage and the Government has never got around to amending them.

Source: *Greenweb Ltd v London Borough of Wandsworth [2008] EWCA Civ 910*

New rules for tree preservation orders

1 October saw the introduction of a new standard application form for consent to carry out work to trees protected by a tree preservation order (TPO). It is a criminal offence to lop, top or fell a tree which is protected by a TPO without the consent of the Local Planning Authority. The form is available from the Department of Communities and Local Government web site at http://www.communities.gov.uk. The application must now include a plan showing the trees.

The procedure for appealing against a TPO or against a notice requiring a tree to be replaced has also been simplified and streamlined and appeals may now be submitted electronically.

Source: *Town and Country Planning (Trees) (Amendment) (England) Regulations 2008*

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FINANCE

Finance matters

by **Catherine A. Stringer**

Receivers have discretion over timing and method of sale

The recent case of *Bell v. Long* concerned the sale of four commercial freehold properties by administrative receivers who had been appointed in respect of a floating charge over the assets of a company, D Limited. The administrative receivers had instructed selling agents to advise on the marketing and sale of the properties. The selling agents marketed the properties individually and together and in due course the properties were sold together as one lot.

Mr. Bell, a director and majority shareholder of D Limited, claimed that the administrative receivers had failed to comply with their duty to the company to obtain the best price reasonably obtainable—he claimed that the price would have been bettered if the properties had been sold individually.

The High Court decided that mortgagees and receivers have a degree of latitude not only as to the timing of any sale but also as to the method of sale. However, once the method of sale is chosen, the property must be properly marketed in an appropriate manner. In addition, mortgagees and receivers can decide when to sell, even if a better price could possibly have been achieved at a later date. In this case, they had taken appropriate advice.

The result: receivers or mortgagees should make sure that they take proper advice on the sale and marketing of assets as well as the timing of the sale and should make sure that all relevant advice and discussions are well documented.

Source: *Bell v. Long & Others [2008] EWHC 1273 (Ch)*

Repeal of financial assistance provisions for private companies

Since 1 October 2008, due to further provisions of the Companies Act 2006 coming into force, a private company may give financial assistance (commonly in the form of a loan, guarantee or security) for the acquisition of its own shares or in relation to the acquisition of shares in a private company parent without having to go through the time-consuming whitewash procedure, which has now been repealed. However, the directors of the company giving the financial assistance must still satisfy themselves on the following points (and be able to show that they have done so):

- the transaction is likely to promote the success of the company for the benefit of its members;
- the proposed financial assistance does not breach rules on distributions or constitute an illegal reduction in the capital of the company; and
- there are no solvency issues.

It should be noted, however, that the law in respect of public companies has not changed, and so a public company still cannot give financial assistance for the purchase of its own shares or those of its holding company, whether the holding company is private or public.

Source: *Companies Act 1985 s 155 – 158; Companies Act 2006, s 1295, Sch 16*

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